FILED
AUG 6 1936
CHARLES ELMORE CROPLEY
CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 260

In the Matter

of

UNITED CIGAR STORES COMPANY OF AMERICA,
Debtor.

CITY BANK FARMERS TRUST COMPANY, assignee of Florence H. Bugbee,
Petitioner,

—against—

IRVING TRUST COMPANY, as trustee of the estate of the above-named debtor, et al.,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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HENRY L. GLENN,
Counsel for Petitioners.

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Of Counsel.

THE COURT PRESS, N. Y. C.

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Respondents.

PETITION FOR A WRIT OF CERTIORARI

To the Honorable Chief Justice of the United States and Associate Justices of the Supreme Court of the United States:

Your petitioner respectfully prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit in the above-entitled case, affirming an order disallowing a landlord's claim under Section 77B of the Bankruptcy Act (quoted *infra,* at p. 13) for "injury resulting from the rejection" of a lease by a trustee in bankruptcy in a bankruptcy proceeding

pending prior to the enactment of Section 77B, where reorganization proceedings under that section were subsequently instituted in such bankruptcy proceeding.

(A) SUMMARY STATEMENT OF MATTER INVOLVED

(a) Facts

Two stipulations of fact constitute the only evidence in the case (R. 19, 33):

Florence H. Bugbee, leased to the debtor (United Cigar Stories Company of America) premises situated in Trenton, New Jersey, for a term commencing April 1, 1926, and expiring March 31, 1946 (R. 23). On August 29, 1932, the debtor filed a voluntary petition in bankruptcy, was adjudicated a bankrupt and abandoned the premises. On November 11, 1932, Irving Trust Company, the trustee in bankruptcy of the debtor, rejected the lease and abandoned the premises. After rejection of the lease, the landlord relet various portions of the premises without notice to the debtor.*

On June 9, 1934, while the bankruptcy proceeding was still pending, the debtor filed in the bankruptcy proceeding, its petition under Section 77B, and on June 14, 1934, the District Court approved the petition as properly filed.

The landlord assigned her claim to the petitioner, agent for the Landlords' Protective Committee in these proceedings, and proof of claim (R. 3) for injury resulting from the rejection of the lease was duly filed by the petitioner, as such assignee.

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* The Special Master, to whom the matter was referred for consideration and report, also found, *sua sponte*, that the landlord had filed in the bankruptcy proceeding "a claim for $1,980.99 for alleged expenditures in restoring a party wall and in closing up a common entrance in the demised premises" (R. 41), though the two stipulations of fact which constituted the only evidence in the case contain no reference whatever to the filing of such claim, or to such restoration.

Irving Trust Company, which had been appointed trustee of the estate of the debtor in the reorganization proceedings, objected to the claim on the ground that the lease, which contained no special covenant for damages or indemnity, had been terminated by the landlord's *reentering and reletting the premises* after rejection of the lease (R. 14).

(b) Rulings of the Courts Below

The Special Master held that Section 77B "could not and did not create any valid and legal claims against the debtor where none existed prior to the enactment of said Section", and that none existed at the time of the enactment of the statute, since the *reletting* of the premises by the landlord had effected a surrender of the lease under the New Jersey law. The Master therefore recommended that the claim be disallowed (R. 37), and his report was confirmed by the District Court (R. 49, 53).

The Court of Appeals affirmed, holding (R. 71) that (1) the injury resulting from rejection of a lease for which a claim is allowable under Section 77B must be "recoverable damages" to which the claimant would be entitled under the applicable state law, and that (2) it was impossible for the petitioner to show that the landlord had "sustained any damages from injury by the rejection of the lease" (R. 73), since, *although under the law of New Jersey the landlord's reentry and reletting of the premises alone had not effected a surrender of the lease,** a surrender had been effected by the landlord's restoration of the premises to the condition they were in at the commence-

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* The rule in New Jersey is different from the rule in New York and some other states. *Liskorsky* v. *Blau*, 114 N. J. L. 324; *Dolton* v. *Sickel*, 66 N. J. L. 492; *Banks* v. *Berliner*, 95 N. J. L. 267.

ment of the term.* A petition for rehearing was denied on May 21, 1936 (R. 75, 83).

(c) Questions Presented

(1) Is a landlord who, after rejection of his lease and prior to the enactment of Section 77B, resumed possession, restored the premises to their original condition, and relet, a "person injured by such rejection", within the meaning of Section 77B, even though under the applicable state law such acts effected a surrender of the lease by operation of law?

(2) If so, is there grave doubt as to the constitutionality of the statute in that respect?

(3) Did the Court of Appeals err in holding that a surrender had been effected because the landlord so restored the premises (in addition to resuming possession and reletting), when the question so decided was not raised by the objection to the proof of claim and the stipulations of fact on which the case was submitted did not mention that the premises had been restored?

(4) Did the landlord's restoration and reletting effect a surrender under the law of New Jersey?

(B) REASONS FOR GRANTING THE WRIT

(1) The question of the proper interpretation of the provisions of Section 77B relating to landlords'

* The Special Master had held that the landlord's reentry and reletting had effected a surrender. He had referred, of his own motion, to the landlord's filing of the claim for restoration merely as "showing that the Landlord, prior to the enactment of Section 77-B, by her reentry and reletting of the premises as aforesaid, considered that the lease [had] terminated and expired", because the entire basis of the claim, in the Special Master's view, was the expiration of the lease (R. 41). See the annexed brief, at p. 22, *infra*.

claims is an important question of federal law which has not been, but should be, settled by this Court.

This Court has in recent years repeatedly recognized the importance of the question of provability of landlords' claims in equity and bankruptcy proceedings (under the old Act), by reviewing on certiorari the following cases: *Miller* v. *Irving Trust Co.*, 296 U. S. 256 (1935); *Irving Trust Co.* v. *A. W. Perry, Inc.*, 293 U. S. 307; *Manhattan Properties, Inc.* v. *Irving Trust Co.*; *Brown* v. *Irving Trust Co.*, 291 U. S. 320; *Kothe* v. *R. C. Taylor Trust*, 280 U. S. 224; *William Filene's Sons Co.* v. *Weed*, 245 U. S. 597 (equity).*

It seems clear that Congress, in including in Section 77B the provisions relating to landlords' claims, intended to change to some extent the rules established by the cases cited. These provisions obviously were patterned upon similar provisions of the English Bankruptcy Acts,** the decisions under which furnish a guide in the interpretation of the new statute. Under the English Acts landlords' claims have uniformly been allowed without regard to the presence or absence of special covenants and without regard to the common law rule that reentry extinguishes the tenant's liability.***

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* Under these decisions, all landlords' claims were held non-provable under the old Bankruptcy Act, whether or not the lease contained a covenant of indemnity and whether or not the landlord reentered before or after the filing of the petition,—except a claim based on a lease containing a liquidated damage clause which became operative *ipso facto* upon the filing of the petition in bankruptcy, as in the *Perry* case, *supra*.

** For instance, paragraph (7) of Section 55 of the English Bankruptcy Act of 1883 (46 and 47 Vict. c. 52) provided:

> "Any person injured by the operation of a disclaimer [rejection] under this section shall be deemed to be a creditor of the bankrupt to the extent of the injury, and may accordingly prove the same as a debt under the bankruptcy."

See also English Bankruptcy Act of 1914, 4 and 5 Geo. V., c. 59.

*** *Ex parte Blake*, 11 Ch. Div. 572; *Ex parte Llynvi Coal & Iron Co.*; *In re Hide*, L. R. 7. Ch. App. 28; *Ex parte Leather Sellers' Co.*, 3 Morrell, 126 (Q. B. D., 1886).

How far Congress intended to go in introducing into the American system the innovation of permitting landlords to share in the assets of the bankrupt tenant urgently requires clarification.

The extent of the litigation which has already arisen in the lower courts over the correct interpretation of these new provisions is shown by the status of claims filed in these reorganization proceedings. 138 landlords' claims filed in these proceedings, totalling $6,185,000,* are now in various stages of litigation. The major question involved in most of these litigated claims is, as in the case at bar, whether termination of the liability of the debtor under the applicable state law, after the bankruptcy or after the rejection of the lease but prior to the enactment of Section 77B, defeats the claim under Section 77B.**

The decision of the Court of Appeals in the case at bar and its decision in *In re United Cigar Stores Co. of America* (*Caroline R. Kuehner and Frederick G. Fischer, as trustees, appellants; Grayson M.-P. Murphy, et al., as a Preferred Stockholders' Protective Committee, et al., cross appellants*), not yet reported (decided by the Court of Appeals on July 14, 1936), are inconsistent with respect to the effect to be given to the local law in determining the validity of a landlord's claim under Section 77B. In the case at bar

* This figure is taken from the trustee's second report on claims dated June 11, 1936 and reflects the three year rent "limitation" prescribed in the statute.

** In many of these cases the leases were not affirmatively rejected by the trustee in bankruptcy, but the landlords accepted assignments of the leases and sub-leases, if any, thus effecting express surrenders, and the landlords also released the debtor from liability under the leases, in some cases reserving their rights with respect to provable claims. In the case at bar no release was given by the landlord nor was any assignment of the lease or sub-leases made by the debtor; nor was there an express surrender of the lease. The decision of the Court of Appeals in the case at bar was that the restoration and reletting of the premises *after rejection* effected a surrender *by operation of law* under the law of New Jersey.

the court held that no claim was allowable under Section 77B unless a valid claim existed under the local law; in the *Kuehner* case the court held that the balance of the claim in excess of three years' rent was not allowable under Section 77B, although perfectly valid under the local law.

The *Kuehner* case also presented other important questions arising under the statute, and, as counsel for the landlords in that case, we expect to file a petition for a writ of certiorari, and the cross appellants may also file a cross petition. That case and the case at bar, arising in the proceedings of this one debtor, present an opportunity for this Court to consider all the more important and difficult questions arising under this new statute with respect to landlords' claims, such as:

(1) Must the rejected lease contain a special covenant for damages or indemnity; (2) if so, does a covenant obligating the tenant to indemnify against loss of future rents entitle the landlord to the present allowance of his claim; (3) what is the effect under the statute of the landlord's reentry after rejection; (4) if such reentry does not defeat the claim, notwithstanding that the tenant's liability is thereby terminated under the applicable state law, is there grave doubt as to its constitutionality in that respect;* (5) what is the effect under the statute if, in addition to reentering, the landlord restores the premises and relets to other tenants; (6) what is the proper method

* The report of the Special Master and the opinion of the District Court in the case at bar show that they were both influenced in their interpretation of the statute by grave doubts as to the constitutional power of Congress to make provision for landlords whose leases had already been terminated prior to the enactment of the statute. That the Court of Appeals was also influenced in this case by similar doubts is indicated by its subsequent opinion in *In re United Cigar Stores Co. (Kuehner and Fischer, appellants), supra* (see annexed brief, p. 20, *infra*).

of liquidation of a landlord's claim,—where the lease contains a covenant to indemnify against loss of future rents and where it does not; (7) to what extent must local rules of law be adhered to in determining the validity and amount of landlords' claims; (8) what is the proper interpretation of the provision of the statute "limiting" landlords' claims to an amount not in excess of three years' rent; and (9) if the statute was intended to cut off entirely the excess of the claim over the amount of three years' rent, for the benefit of the stockholders of the debtor corporation, is the statute to that extent unconstitutional?*

Thus, on the basis of the reorganization proceedings of this debtor, not to mention those of other chain store corporations now pending, it is of substantial importance that this Court should construe the landlord provisions of Section 77B in order that the lower courts may have the benefit of a guide in their decision of the many other cases now pending.

The questions involved in the reorganization proceedings of this debtor are certain to arise in reorganization proceedings of other chain store corporations.** Due to the many locations at which their business is conducted, landlords' claims are apt to consti-

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* A decision of many of these questions under Section 77B will also constitute a precedent with respect to the construction of Section 4 of the Act of June 7, 1934 (48 Stat. 911), which amended Section 63 (a) of the Bankruptcy Act by adding a provision for provability of landlords' claims in bankruptcy liquidation proceedings. The two provisions are substantially similar, as Judge Hand recognizes in his opinion in *In re United Cigar Stores Co.* (*Kuehner and Fischer, appellants*): "This is obvious in §63 (a) (7) and the language there is like that of §77B (b) (10)."

** The extent to which reorganization proceedings have been resorted to by chain store corporations is indicated by the following partial list of such corporations which are now in reorganization under Section 77B in the Southern District of New York alone: Schulte Retail Stores Corporation; D. A. Schulte Inc. of New York; D. A. Schulte, Inc. of Delaware; Huylers, Inc. of Delaware; Huyler's, New York; Schulco, Inc.; H. L. Green Co.; Bellcamp Stores, Inc.; Radio-Keith-Orpheum Corp.; Diamond Brothers Apparel Corp.; Steuben Taverns; Liberty Baking Corp.; Sunnydale Food Stores, Inc.; Highland Dairy Co.; Albrecht's Stores, Inc.

tute the most important and numerous class of claims against such corporations.*

The Court of Appeals itself has recognized, in its subsequent opinion in *In re United Cigar Stores Co. (Kuehner and Fischer, appellants)*, *supra*, the difficulty of construing the landlord provisions of Section 77B.** It is respectfully submitted that the most appropriate time for the construction of these provisions of Section 77B is now, before conflicts in decisions arise in the lower courts and before the confusion arises which existed under the old Bankruptcy Act and finally resulted in applications to this Court for writs many years after the question was first presented to the lower courts.

This Court has recently granted writs to review questions of construction of this new section of the Bankruptcy Act because of its novelty and the difficulty of construing it.***

Some of such corporations which are in reorganization under Section 77B in other districts are as follows: Burg Company (Minn.); H. Winer Co. (Boston); Pollyanna Stores, Inc. (Conn.); Grant Lunch Corp. (Newark, N. J.); Donahoe's Inc. (Pittsburgh, Pa.); Gross Stores, Inc. (Phila., Pa.).

In recently pending reorganization proceedings of two large corporations similar questions regarding landlords' claims were also presented, but such claims were disposed of by compromise: Paramount Publix Corp. (S. D. N. Y.) and J. G. McCrory Co. (S. D. N. Y.)

* 354 of the 481 proofs of claim filed in the reorganization proceedings of this debtor were landlords' claims, amounting to over $13,700,000 (limited to three years' rent) out of a total of all claims of approximately $20,000,000 (Trustee's First Report on Claims).

** Judge Learned Hand said: "It is very difficult to know what the section really means"; "the language is obscure".

*** Writs have been granted in the following cases involving questions under Section 77B:

Nettie Meyer, et al. v. *Kenmore Granville Hotel Company, et al.*, 296 U. S. 565 (whether appeal lies as a matter of right from an approval of a petition for reorganization); *C. S. Tuttle, et al.* v. *Sam Harris, et al.*, 296 U. S. 567 (whether pending foreclosure proceeding is a prior proceeding in an equity receivership); *Theodore Stitt* v. *Reconstruction Finance Corporation*, 296 U. S. 570 (Referee's compensation where proceeding in bankruptcy superseded by 77B proceeding); *Stephen Callaghan, et al.* v. *Reconstruction Finance Corporation*, 296 U. S. 570 (whether compensation for trustees in bankruptcy governed by Section 48, although proceeding superseded by 77B proceeding); *Duparquet Huot & Moneuse Co. et al.* v. *Frysinger Evans, et al.*, 296 U. S. 569 (whether state court foreclosure proceeding is "equity receivership pending" under Section

The decision in the case at bar practically nullifies the obvious attempt of Congress to make provision for landlords whose leases were rejected in bankruptcy proceedings pending at the time of enactment of Section 77B.* It is fair to assume that very few landlords whose leases had been rejected in bankruptcy proceedings prior to the enactment of Section 77B sat idly by and allowed the premises to remain vacant instead of resuming possession and reletting in order to minimize their losses, irrespective of the presence or absence of covenants for damages or indemnity in their leases and irrespective of the effect of reletting on the debtor's liability under the local law.

The extensive existing litigation in the instant proceedings, the probability of similar extensive litigation in the many other reorganization proceedings of chain store corporations now pending, the resulting probable conflict in the future between decisions of the various Courts of Appeal and the difficulty of effecting reorganizations of chain store corporations pending a final determination by this Court of the status of landlords' claims under Section 77B—all these considerations attest the importance of this question, which, notwithstanding the numerous decisions under the old Bankruptcy Act, remains almost as novel and confusing as ever to the courts and to the bar.

77B); *Baxter N. Foust* v. *Munson Steamship Lines*, 80 L. Ed. 746 (whether general restraining order includes pending tort suit although debtor covered by a liability insurance); *Tennessee Publishing Co.* v. *American National Bank et al.*, 80 L. Ed. 957 (whether reorganization plan was properly dismissed as unworkable).

* There can be no doubt that such provision was made in recognition of the known fact that many solvent corporations, particularly chain store corporations, had resorted to bankruptcy during the depression, solely or primarily for the purpose of ridding themselves of liability under their leases (42 Yale L. J. 1003; 33 Col. L. Rev. 231-4; 7 Univ. of Cinn. L. Rev. 164-5; see also the remarks of Representative Celler on the floor of the House, 76 Cong. Rec., Pt. 2, p. 1360, with regard to the debtor in the case at bar).

(2) A writ should also be granted because the Court of Appeals, in basing its affirmance on the landlord's restoration of the premises, when the pleadings and the proof raised no issue as to such restoration, has so far departed from the accepted and usual course of judicial procedure as to call for an exercise of this court's power of supervision and because the procedure of the Court of Appeals in this respect is probably in conflict with the decisions of this Court in *Liberty National Bank* v. *Bear,* 265 U. S. 365, 370-1 and *General Utilities & Operating Co.* v. *Helvering,* 296 U. S. 200, 206.

(3) Moreover, the decision of the Court of Appeals that the landlord could not restore the premises (in order to relet after the tenant's abandonment) without effecting a surrender is clearly in conflict with the applicable local decisions. *Zabriskie* v. *Sullivan,* 80 N. J. L. 673, 676, aff'd 82 N. J. L. 545; *Block* v. *Bell Furniture Co.,* 111 N. J. Eq. 551, 556, 559-561; *cf., Liskovsky* v. *Blau,* 114 N. J. L. 324; *Banks* v. *Berliner,* 95 N. J. L. 267; Schnebly, Operative Facts in Surrenders, 22 Ill. L. Rev. 117, 129. The two cases cited by the Court of Appeals (R. 73) in support of its conclusion to the contrary are not in point. While it cannot be said that this question of local law is of sufficient importance in itself to warrant the granting of a writ, the clear conflict between the decision of the Court of Appeals and the decisions of the New Jersey courts adds weight to the reasons for review already stated.

For the above reasons it is respectfully submitted that this petition should be granted.

CITY BANK FARMERS TRUST COMPANY,
assignee of Florence H. Bugbee,
By ROLLIN BROWNE,
HENRY L. GLENN,
Counsel for Petitioners.

BRIEF IN SUPPORT OF PETITION

OPINIONS BELOW

The opinion of the District Court (per Hulbert, *D. J.*) appears at page 49 of the record and is not officially reported, but is reported in C. C. H. Bankruptcy Law Service, par. 3702. The opinion of the Court of Appeals (per Chase, *C. J.*) is reported in 83 F. (2d) at page 209 and appears in the record at page 71.

JURISDICTION

Jurisdiction to issue the writs is vested in this Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925, c. 229, Sec. 1, 43 Stat. 938, 28 U. S. C. A. Sec. 347 (a). The order for mandate was entered April 13, 1936. A petition for rehearing, seasonably filed on behalf of the petitioners, was entertained by the Court of Appeals and denied by an order entered May 21, 1936 (R. 75, 83).

STATEMENT OF THE CASE

The facts, rulings of the courts below and questions presented are set forth in the foregoing petition.

STATUTE INVOLVED

Subdivision (b) of the Corporate Reorganizations Act (Section 77B of the Bankruptcy Act [48 Stat. 911]) reads in part as follows*:

> "In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding in-

* Other pertinent provisions of Section 77B are quoted *infra*.

stituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of this act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry * * *."

SPECIFICATION OF ERRORS

The Court of Appeals erred in holding:

(1) that the petitioners' claim was not allowable because the liability of the debtor on the lease had been terminated under the applicable state law, after rejection of the lease but prior to the enactment of the statute, by the landlord's restoration of the premises and reletting;

(2) that a surrender had been effected by the landlord's restoration of the premises (in addition to resuming possession and reletting) when the question so decided was not raised by the pleadings or the proof;

(3) that the landlord's restoration and reletting did, under the law of New Jersey, effect a surrender and terminate the liability of the debtor; and

(4) in failing to reverse, with instructions to allow the claim, subject to determination of the amount thereof.

ARGUMENT

POINT I.

The Court of Appeals in misconstruing Section 77B has wrongly decided a new and important question of Federal Law.

The importance of the interpretation of the provisions of Section 77B relating to landlords' claims has been shown in the petition. The extensive litigation surrounding the allowability of landlords' claims under the new statute demonstrates that the status of such claims is even more confusing to the bar and to the courts than under the Bankruptcy Act prior to its amendment.

The conclusion of the Court of Appeals, that the continuing liability of the debtor under the rejected lease is a condition to the allowability of the landlord's claim for the injury sustained by the prior rejection of his lease, arose from a complete misconception of the nature of the *injury* which the statute intended to recognize. The injury suffered by the landlord whose lease is rejected in bankruptcy con-

sists merely in the circumstance that, instead of his lease being assumed and performed according to its terms as a liability of the bankrupt estate, the lease is rejected, the premises are abandoned and the landlord is remitted to the bankrupt corporation for the continued performance of the covenants of the lease. The continued liability of the bankrupt corporation on the lease is of no value and, therefore, of no significance in ascertaining the fact or the extent of such injury.

When the Court of Appeals stated that it was necessary for the injured landlord to prove "recoverable damages as a result of the rejection",* it overlooked the fact that *injury resulting from rejection of a lease in bankruptcy* is an injury which, prior to the enactment of Section 77B, was not known to American law** and gave the landlord no right to recover any damages whatever.

While we recognize that the exact terminology employed in Section 77B is novel and involves difficulties of interpretation, we submit that the opinion of the Court of Appeals in the case at bar and its opinion in the *Kuehner* case reflect a confusion as to the underlying purpose and scope of the statute which could have arisen only from its failure to familiarize

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* The court said in the case at bar (R. 72-3):

> "It was necessary for the appellant to prove recoverable damages as a result of the rejection";

and again: (R. 72):

> "Whether such a claim is allowable under Section 77B * * * depends upon whether, under the applicable state law, it is capable of proof on the merits."

In its opinion in the *Otis* case, the Court of Appeals said:

> "That section does not extend the liability of a lessee beyond what it otherwise would be under applicable law."

** A somewhat similar statute was enacted in Massachusetts many years ago, but apparently has never been squarely passed on by the courts. *Bowditch* v. *Raymond*, 146 Mass. 169.

itself with the English statutes on which the landlord provisions of Section 77B were patterned and the decisions thereunder (see the Petition, *supra,* p. 5).

The mere fact that the injured landlord was given a claim, not for the entire future rent, but only for his injury or damages establishes that it was the intent of Congress that the landlord should resume possession of the abandoned premises and relet them in order to mitigate his damages. Yet, although the law of New Jersey is otherwise (see *supra,* p. 3, footnote), in many jurisdictions reletting by the landlord automatically releases the tenant from further liability, in the absence of an express covenant in the lease continuing his liability after termination. However, the fact that the statute refers to a landlord's claim for injury resulting from rejection of his lease and, in the alternative, to a claim for damages or indemnity under a covenant contained in the lease, shows conclusively that the claim for injury from rejection does not depend upon the presence of a special covenant in the lease.

The decision of the Court of Appeals ignores the clear and unambiguous language of the statute and imposes conditions upon the allowability of landlords' claims which were never intended by Congress. Although many leases do contain special covenants expressly authorizing the landlord to relet the abandoned premises without releasing the tenant from liability, many leases do not contain such provisions. The decision of the Court of Appeals would prevent many landlords whose leases do not contain such special covenants from resuming possession of the premises and reletting them at current rental values, except at the sacrifice of their claims.

Under the decision in the case at bar the landlord would have had to allow the premises to remain idle from November, 1932, in order to preserve the claim under Section 77B, for he could not have relet without restoring the wall between the two buildings and he could not restore without effecting a surrender.

The decision of the Court of Appeals is likely to cause future uncertainty on the subject of allowability of landlords' claims in 77B proceedings. If after the rejection of a lease in a pending bankruptcy proceeding the landlords' re-entry and reletting prior to the enactment of Section 77B and the filing of the tenant's petition thereunder defeats the claim in a 77B proceeding, then the landlord's re-entry and reletting after the filing of the tenant's petition under Section 77B and the rejection of the lease by the reorganization trustee (where there has been no prior bankruptcy proceeding) and at any time before the end of the term or at least before the confirmation of a plan, would similarly be deemed to defeat the claim. The language of the opinion in the case at bar makes no distinction between rejection before the statute and rejection after the statute. Moreover, no distinction is made by the statute between a lease rejected by the trustee in the reorganization proceeding and one previously rejected by a bankruptcy trustee in a proceeding pending at the time of the institution of the 77B proceeding (see provision quoted *supra,* p. 13). In either case the "person injured by such rejection" is, without any qualification, "deemed to be a creditor" for the purpose of the plan and its *acceptance.*

Where the rejection occurred prior to the enactment of Section 77B in a bankruptcy proceeding still pending at the date of its enactment, and the tenant then filed its petition for reorganization in the bankruptcy proceeding, as the statute provides that it might do, the language making a person injured by

such prior rejection a creditor must mean a creditor of the *assets in the bankrupt estate* with which the debtor is revested upon the filing of the petition under Section 77B, which became in turn the reorganization estate. The fact that the injury referred to is that resulting from the release of such estate from liability for rent makes it clear that any action the landlord took in the interim which had the effect of terminating the liability of *the bankrupt corporation* on the lease is entirely immaterial.

The fact that reletting would release the bankrupt tenant under the law of some states was of no significance to landlords under the old Bankruptcy Act, for they could not share in the bankrupt estate under the old Bankruptcy Act and their rights against the bankrupt corporate tenant were worthless. Since Congress must have known that and in view of the absence of any distinction in the language of the statute between rejection prior to the enactment of the statute and rejection after the enactment of the statute, Congress must have intended that a reletting by the landlord prior to the enactment of the statute should not defeat the claim against the estate, no matter in what state the premises should be located.

This conclusion is confirmed by both the language and the legislative history of the statute. The landlord's claim is measured with reference to the date of "surrender of the premises to the landlord or * * * reentry of the landlord, whichever first occurs, * * * whether *before or after* the filing of the petition". Thus, it is clear that reentry before the filing of the petition for reorganization does not defeat the claim, although, under the law of many states, the landlord's reentry terminates the lease and releases the tenant from further liability.

Section 77B, as it originally passed the House, con-

tained a provision conditioning allowability of a landlord's claim upon his not having terminated the lease by reentry or otherwise. That provision was eliminated while the bill was pending in the Senate. (See H. R. 5884, 73rd Cong., 1st Sess., June 2, 1933 [p. 10]; 78 Congressional Record, 8109, 73rd Cong., 2nd Sess.; H. R. 5884, Print of May 7, 1934 [p. 11] H. R. No. 1821, 73rd Cong., 2d Sess. [p. 2]). The elimination of that provision, and the insertion in place thereof of the provision measuring the landlord's claim with reference to the date of his *reentry,* whether *before* or after the filing of the petition, clearly shows the actual intent of Congress that the claim should be allowed despite the termination of the lease, after its rejection, by reentry or other action of the landlord effecting a surrender by operation of law.

The intention of Congress as expressed in Section 77B and the contemporaneous amendment to Section 63 (a) was to change the rule of the *Manhattan Properties* case and provide for a new "division of the pot" of the tenant's estate in all bankruptcy proceedings pending at the date of the enactment of the Act of June 7, 1934 (a) in which the time for filing claims had not expired or (b) in which reorganization proceedings should thereafter be instituted. In neither case did Congress create a *substantive* right not theretofore existent. The leases were valid obligations of the landlord at the time of the institution of the original bankruptcy proceedings, and the statute merely corrected the injustice inherent in the former rule, so far as pending proceedings were concerned.

The Special Master (R. 39), the District Court (R. 50), and the Court of Appeals* were all influenced in

* Although the Court of Appeals made no reference in its opinion in the case at bar to its doubts as to the constitutionality, it is clear that it was influenced by such doubts because of the language used in its subsequent opinion on the claim of *Kuehner and Fischer, supra,* in which, in

their interpretation of the statute by their doubts as to the constitutional power of Congress to make provision for landlords whose leases had already been terminated.

Reference is respectfully made to the brief of *Amici Curiae* Godfrey Saxe and John Gerdes for a fuller discussion of the proper interpretation of the statute and of its undoubted constitutionality if construed as contended for.

POINT II.

The Court of Appeals, in deciding an issue not raised either by the pleadings or proof below, departed from the usual course of judicial procedure and decided a question of Federal procedure in conflict with the decisions of this Court.

As we have seen, the trustee's objection to the claim (R. 14) raised simply one narrow issue of local law,—to-wit, whether the landlord's *reentering and reletting* terminated the debtor's liability under the lease, no point having been made of the landlord's *restoration* of the premises to their former condition. Moreover, the stipulations of fact, which were drawn in the light of the sole issue raised by the trustee's objection, contained no reference whatever to the restoration of the premises or the filing of a claim for the expense thereof.

Even assuming that the Special Master had the right to take judicial notice of the landlord's filing

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speaking of a claim for "injury resulting from the rejection", it said: "But, whatever was meant, we cannot suppose that Congress was trying to make over the contract by imposing a liability for future rent on the lessee after the term had ended. Indeed, we should have considerable doubt whether the bankruptcy power would support such a method."

of a claim in the prior bankruptcy proceeding,* although not requested to do so by any party, the "finding" of the Special Master was simply that the landlord had filed a claim for the expense of restoration. His conclusion from this finding was that the filing of such a claim indicated that the landlord thought the lease had been terminated by her previous reentry and reletting because the debtor was under no obligation to restore until the expiration of the term.** He did not even consider whether the restoration itself was a factor bearing on the question of whether a surrender had been effected. He limited his report to the question raised by the objection to the proof of claim and the stipulated facts. The opinion of the District Court was similarly limited (R. 49).

The Court of Appeals, however, seized on the Special Master's "finding" that a claim for reimbursement of the expense of restoration had been filed and drew from it inferences of further facts,—to wit, that the repairs made by the landlord upon resuming possession were "structural changes" (R. 72), or "substantial changes in the premises" which were "indicative of the resumption of the dominion of them inconsistent with the continued status of landlord and tenant under the lease" (R. 73), and, by implication, that the repairs made by the landlord were not necessary for the preservation of the premises or in order to relet.

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* The Special Master's report (R. 41, fol. 123) states that "the stipulation herein shows that this claim [for restoration] is also asserted in this Reorganization proceeding", but the Special Master was mistaken in this respect, as the stipulations of fact upon which the case at bar was submitted (R. 19, 33) contain no reference to the filing of a claim for restoration either in the bankruptcy proceeding or in the reorganization proceeding.

** This conclusion, which was not approved by the Court of Appeals, was erroneous, since the claim was provable, if at all, only on the theory that the bankruptcy petition constituted an anticipatory breach of the agreement to restore. *In re Metropolitan Chain Stores*, 66 F. (2d) 485, 487; *Possart* v. *Irving Trust Co.*, 68 F. (2d) 807.

Under the law of New Jersey, the burden of proving facts showing a surrender rests on the party alleging surrender. *O'Neal* v. *Pearse*, 87 N. J. L. 382, aff'd 88 N. J. L. 733. If the trustee's objection had raised the issue that the landlord's action in making certain repairs had effected a surrender, the trustee would have been required to prove, or the petitioner could have caused to be inserted in the stipulation of facts, the details with respect to the repairs made by the landlord. As we shall show, if the record had definitely shown that the repairs made were necessary to preserve the premises or to make them rentable, the Court of Appeals must have held that no surrender had been effected (see *infra*, p. 25). All these considerations were ignored by the Court of Appeals when it decided this question without pleadings and without evidence, and without the Special Master's or District Court's having passed upon the question.

In thus proceeding, the Court of Appeals has ignored the elementary principles that appellate courts should limit their consideration of cases to issues properly framed and passed upon by the courts below, and to evidence regularly produced, and also has ignored applicable decisions of this Court. *Liberty National Bank* v. *Bear*, 265 U. S. 365; *General Utilities & Operating Co.* v. *Helvering*, 296 U. S. 200. See also *Helvering* v. *Salvage*, 297 U. S. 106 and *Compañia General* v. *Collector*, 279 U. S. 306.

This Court held in *Liberty National Bank* v. *Bear* that where neither the trustee's objection to a claim nor the proof introduced by it raises an issue of law, the Court of Appeals could not base its affirmance of an order disallowing the claim on such issue, but should have reversed. The trustee had objected to the claim on the ground that the judgment securing it

had been recovered within four months prior to bankruptcy, but had not alleged nor proved that the bankrupt was insolvent at that time. Similarly in the case at bar the trustee neither alleged nor proved the nature of the repairs made by the landlord nor alleged that the making of such repairs had effected a surrender.

See also the opinion of this Court in the *General Utilities & Operating Co.* case, *supra,* in which it was said (p. 206):

> "The second ground of objection, although sustained by the court, was not presented to or ruled upon by the Board. The petition for review relied wholly upon the first point; and, in the circumstances, we think the court should have considered no other. Always a taxpayer is entitled to know with fair certainty the basis of the claim against him. Stipulations concerning facts and any other evidence properly are accommodated to issues adequately raised."

POINT III.

The Court of Appeals, in holding that the restoration and reletting effected a surrender, has decided a question of local law contrary to the applicable local decisions.

Nothing in the record indicates that the restoration of the party wall and the closing up of the common entrance were not repairs which were required to preserve the building or to enable the landlord to relet the building as an independent unit for the account of the debtor. On the contrary, the only inference

that can be drawn from the report of the Special Master as to the nature of the repairs is that the debtor occupied the premises involved herein and the adjoining premises as one unit. Otherwise, the debtor would not have cut a common entrance nor have torn down the party wall between the two buildings. The further inference necessarily follows that Mrs. Bugbee, upon the debtor's default, was compelled to restore the party wall and close up the common entrance in order to prevent such injury as might otherwise result from the separate occupation of the adjoining premises either by the debtor or by a new tenant. The New Jersey decisions clearly hold that repairs made by a landlord upon his tenant's abandonment for the purpose of preserving the premises from injury do not effect a surrender of the lease, even when accompanied by reletting. *Meeker* v. *Spalsbury,* 66 N. J. L. 60; *Liskovsky* v. *Blau,* 114 N. J. L. 324; *Banks* v. *Berliner,* 95 N. J. L. 267; *Block* v. *Bell Furniture Co.,* 111 N. J. Eq. 551, 559.

Assuming, *arguendo,* that the repairs made by the landlord in the case at bar were not necessary to preserve the premises under the doctrine of these cases, it is clear that where the repairs made by the landlord go no further than to restore the premises to their original condition, the repairs so made do not effect a surrender, even when accompanied by reletting. *Zabriskie* v. *Sullivan, supra.* This rule appears to be of general application in states where reletting alone does not effect a surrender. 22 Ill. L. Rev. 117, 129, *supra.* Any other doctrine would nullify the New Jersey rule that a landlord may relet for the tenant's account (see cases cited *supra,* p. 3, footnote), since the privilege is worthless unless the landlord may put the premises in rentable condition. It is ap-

parent that the premises in the case at bar could not have been relet as an independent unit without four walls and their own private entrance, and that the landlord's repairs were necessary in order to enable her to relet. Neither principle nor common sense required the landlord to try to relet the premises to such new tenant as might ultimately lease the adjoining premises, even if that had been possible.

Respectfully submitted,

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